



Taxation and state-building: The tax reform under the Nationalist Government in China, 1928–1949



Yin Xu ^{a, *}, Xiaoqun Xu ^b

^a School of Accountancy, Strome College of Business, Old Dominion University, Norfolk, VA 23529, USA

^b Department of History, Christopher Newport University, 1 Avenue of the Arts, Newport News, VA 23606, USA

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ABSTRACT

Using primary sources and drawing on insights from the new accounting history and the new fiscal sociology, this paper examines the tax reform launched by the Nationalist Government in China during 1928–1949 as a case study to enrich an understanding of the relationship between taxation and state building. Among other things, the paper reveals a shift from the traditional Confucian ideology of “low taxes” to the Western-derived ideology of “good taxes,” used by the state to justify new taxes. It discusses how the Chinese Civil War and the Sino-Japanese War differently affected the Nationalist Government’s political legitimacy and state finance and taxation. It analyzes how tax compliance was pursued by the Nationalist Government through state-society negotiations and compromises over taxation, in the absence of representative political institutions, as well as coercive enforcement of tax laws and regulations—the two approaches together actualized and delimited the new tax regime and the growing state power (legitimacy and capacity). These history/culture-specific features may be understood as variations to a general historical pattern of taxation and state building based on European-American experiences.

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1. Introduction

Research on accounting history, especially “the social science-influenced ‘new accounting history’” since the mid-1980s (Napier, 2006, p. 468), has greatly broadened our understanding of the role of changing accounting techniques and the rise of the accounting profession in, and their interactions with, the political, economic, technological, and social changes or changes in government regulations, accounting rules, economic organizations, and societies at large over time and space around the world (see Napier, 2006; Cooper & Robson, 2006; Burchell, Clubb, & Hopwood, 1985). In this broad scholarly development, one important but still understudied area of research is taxation as accounting history. Based on primary sources, the present study is to enrich the literature with an analysis of how tax systems developed in tandem with modern transformation of the state in early twentieth-century China.

A body of scholarship on taxation and state building in Western countries has formed a general historical understanding: The emergence of modern states in Europe was manifested first and

foremost in the increasing power of a central government, either a monarchy or otherwise, to tax people and economic activities across the territory it ruled. Historically, wars and commerce played a key role in the rise of the “tax states” or “fiscal states”. In the process of taxation, the legitimacy and capacity of the state would reinforce one another and grow hand in hand. The growing state legitimacy involved imposing new taxes or higher rates of taxes and promulgating and enforcing tax laws, which taxpayers were persuaded or compelled to accept and comply with. The growing state capacity was manifested in the evolution and expansion of tax collection apparatus from tax farmers and other amateurish, part-time operators to full-time, salaried tax professionals who were trained for and made their careers in this growing field of state functions.¹ In short, successful imposition and collection of taxes by a centralized authority was one of the essential features of state making or state building (e.g., Tilly, 1975, 1985; Braun, 1975; Webber & Wildavsky, 1986; Brewer, 1990; Kiser & Schneider,

¹ A tax farmer was a private person or entity that pays the ruler or the state a fee in return for the right to collect taxes on behalf of the ruler or the state. An alternative was for the private person or entity to pay in advance an amount of money that was expected from the taxes to be collected, usually at a discount for collection cost and profit.

* Corresponding author.

E-mail addresses: yxu@odu.edu (Y. Xu), xxu@cnu.edu (X. Xu).

1994; Bonney, 1995; Douglas, 1999; Yun-Casalilla, O'Brien, & Comin, 2012).

How would this historical pattern apply to China where a centralized imperial dynasty was founded over two millennia ago and succeeded by many, but the significant transformation of state and society into modern forms took place in the twentieth century? If the pattern is applicable to modern China, were there any history/culture-specific features or variations? How did taxation actually interact with modern state building in the Chinese context? These questions have not been squarely addressed in the scholarship. This paper seeks to fill that lacuna by examining a crucial moment in China's experience of taxation and state building, i.e., the tax reform under the Nationalist Government during 1928–1949.

After the fall of the last imperial dynasty, the Qing (1644–1911), and the founding of the Republic of China in 1912, the promise of a functioning parliamentary government was quickly turned into a deep disillusionment for Chinese citizens. With the passing of the authoritarian presidency of Yuan Shikai in 1916, warlords dominated the political scene, fighting one another for the control of the national capital and various provinces and revenues there. China's domestic disorder did not help its international standing. It failed to recover full national sovereignty from the unequal treaties with Western Powers and Japan dating back to the nineteenth century. Japan stepped up its encroachment on mainland China by taking over the German leasehold in Shandong province and imposing the Twenty-One Demands on China in 1915. China's failure to regain the German leasehold in Shandong at the Paris Peace Conference in 1919 set off a high tide of Chinese nationalist movement with twin goals of anti-imperialism and anti-warlordism. It culminated in a military campaign against warlords led by the Nationalist Party and the founding of the Nationalist Government in 1927. In the meantime the Chinese Communist Party (CCP) was founded in 1921 as a participant in the nationalist cause, with a Marxist-Leninist ideology. The Nationalist Party-Government initially cooperated with the CCP (1924–1927) and then turned against it. Through a prolonged civil war, suspended during the Second Sino-Japanese War (1937–1945) and resumed in 1946, the struggle between the Nationalist Government and the CCP resulted in the latter's victory and the founding of the People's Republic of China in 1949.

Given the turbulent history sketched above, it is not difficult to understand that in the first half of the twentieth century, while searching for a modern form, the Chinese state was under severe financial strains and constantly struggling with revenue extraction. After the Nationalist Government came to power in 1927, it began to reform the tax system, preceded by a recovery of tariff autonomy and a currency reform. From 1936 to the late 1940s the government instituted new categories of taxes, including income tax (both personal and business), estate tax, stamp tax (for print matters), and business tax.

Through examining how the tax reform unfolded, this paper makes empirical and theoretical contributions to the accounting history literature. Empirically, this is another case study, based on primary source research, of the relations between taxation and state building in one of the major non-Western countries. In the past fifteen years or so the literature has seen several studies on taxation, such as tax assessment and collection in ancient Egypt (Ezzamel, 2002), the emergence of the Exchequer in medieval England (Jones, 2010), assessment and accounting of profit income tax in mid-nineteenth century England (Lamb, 2001), the resistance to the whiskey tax of 1791 in the United States (Krom & Krom, 2013), and the increase of stamp tax on newspapers in Britain during the French Revolutionary War (Oats & Sadler, 2004). Overall, however, studies on “taxation framed as accounting historical research” (Lamb, 2003; also see Lamb & Lymer, 1999) remain to be strengthened. The present study adds a significant piece to the

literature.

Theoretically, the paper draws on insights and findings from the “new accounting history” (Napier, 2006) and the “new fiscal sociology” (Martin, Mehrotra, & Prasad, 2009) and applies them, with modifications, to a country-specific case to reach additional insights into the relations between taxation and state building. Consistent with the findings in the previous literature, this paper explicitly treats state building as growth of state legitimacy and capacity or state power, and treats taxation as state building (or an integral part of state building), not just for state building or vice versa. The paper engages the “theory of predatory rule” (Levi, 1988). On the one hand, it uses concepts from the theory such as the state/ruler's bargaining power, transaction costs, and discount rate (see the Literature review section below), and on the other hand, it differs from the theory in two important aspects illustrated by the Chinese case. First, it analyzes how ideology on taxation as discursive resource added to the state's political resource or bargaining power, and second, it analyzes how Chinese state-society negotiations and compromises over taxation, in the absence of representative political institutions typical of Western experiences, both actualized and delimited the growth of state power in Nationalist China. At the same time, the paper supports an important viewpoint in the literature, i.e., how civil war and international war—in our case the Chinese Civil War and the Second Sino-Japanese War—differently affected state legitimacy and state finance and taxation.

The rest of the paper is organized as follows: Section 1 “Literature on Taxation and State Building” reviews relevant literature in the new accounting history and the new fiscal sociology and situates this study in the literature; Sections 2 “Finance & Taxation in Late Imperial & Early Republican China” provides a historical background for our case study; Section 3 “A New Ideology on Taxation” deals with the shift from the Confucian ideology of “low taxes” to the Western-derived one of “good taxes” to justify tax reform under the Nationalist Government; Section 4 “New Taxes and Revenue Increase” discusses the adoption by the state of new categories of taxes and the resulting revenue increase; Section 5 “Taxation as State Building” looks into the growth of state legitimacy and capacity through building tax apparatus and training and monitoring tax agents; Section 6 “State–Society Interactions over Taxation” analyzes the state's efforts at tax compliance through state-society negotiations as well as enforcement of tax laws and regulations, which manifested a particular political ecology in a non-Western society. A brief conclusion will summarize our findings.

2. Literature on Taxation and State Building

Tax research as accounting history benefits from the intellectual concerns and theoretical approaches of the new accounting history and the new fiscal sociology. As Napier (2006) has outlined, unlike the traditional views of accounting, the new accounting history pays greater attention to the social environment with which accounting interacts, manifesting several research concerns. First of all, from its perspective, “accounting is not just reflective but constitutive: it is not merely a passive effect of its environment but works to shape this environment. The constitutive power of accounting arises not just in the context of the individual organization, but also in a wider social context” (Napier, 2006, p. 456). Secondly, it re-conceives what accounting was in different historical circumstances. With an “anti-essentialist” nature, it has “an awareness that the bundle of practices (calculative or otherwise) that happened to be labeled as accounting at any point in time and space is contingent (delineating a specific bundle and documenting the conditions of its emergence provides a problem for historical

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